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## RESEARCH

## Summary:

**California Department Of Veterans Affairs; General Obligation; General Obligation Equivalent Security; Other; Single Family Whole Loan**

**Publication date:** 19-Feb-2009  
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## Credit Profile

California Department of Veterans Affairs Home Purch rev bnds ser 2005 A

<i>Long Term Rating</i>	AA-/Stable	Affirmed
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California Department of Veterans Affairs Veterans General Obligation bnds ser CA/CB dtd 04/01/2005 due 12/01/2034

<i>Long Term Rating</i>	AA-/Stable	Affirmed
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**California Dept of Vet Affairs, California**

California

**California Dept of Vet Affairs veterans GO bnds ser BJ 7/8 (AMT) rmkted dtd 12/01/1999 due 12/01/2002-2016 2018 2024 2032**

<i>Unenhanced Rating</i>	AA-(SPUR)/Stable	Affirmed
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**California Dept of Vet Affairs vets GO bnds ser BX-1 dtd 06/01/2001 due 12/01/2005-2013 2020 2024-2025 2031-2032**

<i>Unenhanced Rating</i>	AA-(SPUR)/Stable	Affirmed
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## Rationale

Standard & Poor's Ratings Services affirmed its 'AA-' long-term rating and underlying rating (SPUR) on the California Department of Veterans Affairs' outstanding veterans home purchase revenue bonds and general obligation (GO) bonds. The rating is based on our assessment of the credit strength of the Veterans Farm and Home Building Fund of 1943 (1943 Fund).

Credit strengths of the fund include our opinion of:

- The very high asset-to-liability parity of 110% as of June 30, 2008;
- The very strong performance of the contracts of purchase and investment securities; and
- The resiliency of cash-flow projections.

Offsetting factors include our view of:

- The low net income of the resolution, which has been negative in all years except fiscal 2007;
- An interest rate mismatch between the fund's assets and non-callable GO bonds;
- The exclusive use of Radian Guaranty, Inc. as the primary mortgage insurance provider on 30% of the loans; and
- A weakening California residential real estate market.

The GO bonds are secured by the full faith and credit of the state of California, and have an effective senior lien on the 1943 Fund. The revenue bonds have a junior lien on the 1943 Fund. Cash flows indicate the fund has the ability to pay all debt service in a full and timely manner in accordance with bond documents while retaining a sufficient overcollateralization level

that is commensurate with the rating on the bonds. The 1943 Fund posted a net loss of \$3.5 million in fiscal 2008, which was its second-best performance during the last five years. The fund has more than \$220 million in equity, which we believe is enough to pay all debt service through maturity. The fund also has \$111 million in non-callable, high rate debt, which has been a drain on profitability for many years. By 2010, when the department's high-rate non-callable bonds mature, we expect the indenture to show consistent and significant positive net income.

The loan portfolio consists of more than 13,000 contracts of purchase; 30% have insurance from Radian Guaranty (BBB+/CWNeg), 14% are guaranteed through the Veterans' Administration, and 57% are uninsured with a loan-to-value ratio of no more than 80%. Delinquency as of Sept. 30, 2007, was 2.68%, lower than the 4.81% for the state of California for a similar loan portfolio.

Despite the exclusive use of Radian as mortgage insurance provider, in our view the resolution can withstand foreclosure assumptions for a 'AA' indenture in a large state. We believe the asset position of the indenture enables it to maintain uninterrupted payment of debt service, assuming no recovery of mortgage insurance claims from Radian.

In our opinion, strong underwriting standards have benefited the fund. During the past five years, the average credit score of borrowers has been 721 (FICO) and the department finances only fixed rate, fully amortizing loans. The department services all its loans. California housing markets are still showing dramatic declines in construction activity and prices. The Office of Federal Housing Enterprise Oversight's home price index for the third quarter of 2008 showed California ranked worst in the country, with average year-over-year declines of 21%. According to the data provided by the Mortgage Bankers Association, subprime and prime mortgage foreclosure rates in California have strongly diverged from one another during the second quarter of 2008. State-wide, 16.8% of subprime mortgages (compared with 11.81% nationally) entered foreclosure, while 1.96% of prime mortgages entered foreclosure (compared with 1.42% nationally). With these rates, California ranked second highest in the subprime and fourth highest in prime foreclosure rate in the nation.

## Outlook

The stable outlook reflects our view of the anticipated stability of the 1943 Fund assets and revenues as well as its sufficiency to withstand programmatic losses during the long term. Should the offsetting credit weaknesses decline along with a stable trend of positive net income, we believe positive rating action could result.

### Ratings Detail (As Of 19-Feb-2009)

California Dept of Vet Affairs home		
<i>Long Term Rating</i>	AA-/Stable	Affirmed
California Dept of Vet Affairs home purch rev bnds		
<i>Long Term Rating</i>	AA-/Stable	Affirmed
California Dept of Vet Affairs General Obligation ser 2007CE dtd 12/06/2007 due 12/01/2042		
<i>Long Term Rating</i>	AA-/Stable	Affirmed
California Dept of Vet Affairs Home Purchase		
<i>Long Term Rating</i>	AA-/Stable	Affirmed
California Dept of Vet Affairs Veterans GO		
<i>Long Term Rating</i>	AA-/Stable	Affirmed
California Dept of Vet Affairs Veteran Home Purchase rev bnds ser 2007B		
<i>Long Term Rating</i>	AA-/Stable	Affirmed
<b>California Dept of Vet Affairs home purch rev bnds ser 1997A/B</b>		
<i>Unenhanced Rating</i>	AA-(SPUR)/Stable	Affirmed
<b>California Dept of Vet Affairs home purch rev bnds ser 2002A dtd 03/06/2002 due 12/01/2021 2027</b>		
<i>Unenhanced Rating</i>	AA-(SPUR)/Stable	Affirmed
<b>California Dept of Vet Affairs, California</b>		
California		
California Dept of Vet Affairs go bnds		
<i>Long Term Rating</i>	AA-/Stable	Affirmed
<b>California Dept of Vet Affairs (California) veterans GO bnds series BG &amp; BH</b>		
<i>Unenhanced Rating</i>	AA-(SPUR)/Stable	Affirmed
<b>California Dept of Vet Affairs (California) vets GO bnds (California) ser BY &amp; BZ dtd 12/01/2001 due 12/01/2017 2021 2024</b>		

<i>Unenhanced Rating</i>	AA-(SPUR)/Stable	Affirmed
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**California Dept of Vet Affairs (California) GO**

<i>Unenhanced Rating</i>	AA-(SPUR)/Stable	Affirmed
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**California Dept of Vet Affairs, California**

California

California Dept of Vet Affairs, California

California Dept of Vet Affairs go bnds ser BV & BW dtd 04/01/2001 due 12/01/2005-2013 2018-2020 2024-2025 2028-2029 2032

<i>Unenhanced Rating</i>	AA-(SPUR)/Stable	Affirmed
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Many issues are enhanced by bond insurance.

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